



When Times Get Tough Just Borrow More Money

Posted by **Pierluigi Oliverio** on Monday, February 22, 2010

Mayor Reed shared a candid and honest view of city revenues and expenses at the State of the City Breakfast last week. (Personally, I miss the State of the City speeches in the evening as it led to dinner after the speech and spending money Downtown.)

As we already know the City is walking the plank, with the sharks swimming below in the ocean (sharks = bankruptcy) and a sword wielding pirate (pirate = hard choices) is forcing us to walk down the plank off the ship. Walking back up the plank is not an option unless tough decisions are made now. However it seems that another alternative being heard more and more at city hall is borrowing.

This week the council will vote on an RDA budget that proposes to borrow \$10 million from the Park Trust Fund, Ice Center and Water Pollution Control Plant to be repaid in approximately six years. Six years of risk. What if there is a major repair needed at the Water Pollution Control Plant or the Ice Center?

Six years of not being able to make a strategic purchase of property for a park or trail connection. The Park Trust Fund comes from fees paid by housing developers who build market rate housing (affordable housing is exempt from paying park fees). In turn, they want to see their money spent on what it was intended...parks! Actually if we do not spend Park Trust Fund money within a certain amount of time the city must return the money.

The Library Parcel Tax reserves were considered for borrowing but spared since it would kill the chance of getting the voters to continue the tax in 2012. (A point I brought up at the Neighborhood Services Committee.) The alternative to borrowing this \$10 million would be to borrow this amount from the Housing Department as allowed by the State Legislature, which I support.

Borrowing of these funds today limits the city's options tomorrow when the state will grab more money from the city. If we are forced to borrow then let's do it to maintain core services like police and libraries, not more affordable housing, most of which does not pay property tax.

The City will also be issuing \$25 million in commercial paper to pay a portion of the State's raid of San Jose RDA. Commercial paper is the equivalent of a home equity line that must be paid back. The collateral for the \$25 million in commercial paper is our beautiful California Theater, home of San Jose Opera

and Symphony Silicon Valley. Again the other option would be to borrow this money from the Housing Department instead of borrowing more on our equity line. Borrowing in both cases is due to the State Legislature taking \$75 million away from San Jose RDA funds.

At the budget study session last week a union lobbyist touted the idea of risky pension obligation bonds. Pension Obligation Bonds (more borrowing) are used to fund the unfunded liability of pensions, so as to lessen the large amounts coming out of the general fund in future years when there will be losses. This year \$38 million is being transferred from the general fund to cover the pension investment losses which is equivalent to over 200 police officers or staffing for 17 fire stations or paving 24 miles of road. This arbitrage scheme would have the city issue taxable bonds at say 6 percent and then take that money and invest it with the city Retirement Funds. The hope is that the city Retirement Funds would have a greater rate of return than the 6 percent we would have to pay the bondholders. In the last 10 years the average rate of return for city Retirement Funds has been 4.4 percent. (While doing my taxes on Valentines Day I noticed my own mutual funds had returned 3.5% percent over 10 years.)

If the Retirement Fund investments do not perform over time then we could lose more money or possibly break even or make a higher return. Positive investment returns would be restricted to paying off future retirement liability. I think outside of the risk, Pension Obligation Bonds may give the council a reason to not seek second tier retirement benefits the taxpayer can afford for new employees.

The other idea suggested by the union lobbyist was bonding construction and conveyance tax (C&C) funds so that we could spend more now so cuts do not have to be as deep. There again you have to gamble on the future tax receipts and the total amount of C&C funds will shrink since you have to pay the costs associated with bonds. However this borrowing would allow the Council to avoid the question of outsourcing.

It is just another day in local government. Perhaps one way to raise money for the city is to sell bumper stickers that read, "Why do today what you can put off 'till tomorrow?"

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